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SUBJECT: OUR ANTI-CORRUPTION STRATEGY AND THE MCC: CAN WE
HELP PREVENT CAMBODIA FROM BECOMING THE NIGERIA OF S.E.
ASIA?

¶1. (U) This message contains an action request. See
paragraph 11.

¶2. (SBU) Summary. Corruption in Cambodia is systemic and pervasive, and one of the country's key challenges to surmount if its economic profile is to continue to grow in a positive manner. Transparency International ranked Cambodia 151 out of 163 countries on its corruption scale in 2006, placing Cambodia behind its other S.E. Asian neighbors save for Burma. The discovery of extractable resources, not only oil and gas, but gold, bauxite and other minerals presents an opportunity to create a management regime that is transparent and assist the Cambodian people to a better life -- but only if we and other donors can press the Cambodian government (RGC) to take ownership of the anti-corruption issue. The Mission has a multi-dimensional strategy for fighting corruption and our technical assistance has brought the draft anti-corruption law closer into line with international standards, forged a coalition of NGOs involved in the issue, and trained journalists in investigative journalism. In the second phase (2007-2010), we will seek ways to support policy and regulatory reform to prevent the "oil curse," instituting measures to ensure greater transparency of information. In order to convince the Cambodian leadership that it is in their interest to eliminate graft, we want to demonstrate that there will be rewards if they adopt reform measures. The Millennium Challenge Corporation (MCC) is one possible carrot that would appeal to reform-minded RGC leaders and those seeking stronger ties with the United States; the Ambassador strongly supports an MCC visit to Cambodia to brief senior RGC leaders on the MCC's threshold program. End Summary.

The Nature of Corruption in Cambodia

¶3. (U) Corruption in Cambodia is systemic and pervasive. Every Cambodian and most foreigners have to deal with it on a daily basis and every person who is a part of the political/economic system cannot escape participating in corruption. Participation ranges from the student paying his teacher for lessons and sometimes to pass a course to paying off policemen on the street for real or imagined traffic offenses, paying the fire department to put out a fire, to paying a judge for a favorable legal verdict. Private businesses are required to pay unofficial fees often related to "inspections" of the businesses by various government ministries and agencies, which are usually simple pretexts for demanding money. A USAID-commissioned survey conducted by the Economic Institute of Cambodia (EIC) in 2006 found that in the previous year, enterprises that were surveyed paid about 2.8 percent of their annual turnover in

"unofficial fees", or a total of approximately \$330 million paid by firms in the private sector. This amounted to about six percent of Cambodia's GDP in 2005. The high rate of unofficial fees paid to government officials also affected tax collection severely. The EIC study determined that the Tax Department collected only about 25% of potential taxes in 2005, representing a loss of about \$400 million to the national budget.

¶4. (U) Corruption is aided by the lack of transparency in government. For example, many ministries are currently in the process of selling the valuable government land in the middle of Phnom Penh and moving to cheaper sites on the outskirts of the city. However, there is little public discussion of these moves, no public tender, nor is there publicly available information on the profits being made or the destination of those profits. This lack of transparency has contributed to the damage that Cambodia's reputation has suffered as a result of corruption. Transparency International ranked Cambodia 151 out of 163 countries on its 2006 scale of the prevalence of corruption in the perceptions of business people and analysts. Ranking Cambodia's competitiveness, the World Economic Forum placed Cambodia at 112 of 117 countries in its 2005 survey. Eighty percent of respondents cited corruption as the principal reason for low ranking Cambodia. The prevalence of corruption and especially its effect on the legal system has without a doubt inhibited foreign investment in Cambodia. U.S. investment, despite the government's adoption of measures to attract investors, has lagged behind other countries. The U.S. was the tenth largest investor in Cambodia in 2005 (about \$5 million) and the sixth largest in 2006 (\$62 million).

Extractive Industries: More Resources for Corruption

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¶5. (U) Cambodia's relatively low GDP (\$6.5 billion in 2006) has restricted the scale of corruption somewhat in past years. However, its growing economy (averaging over 10% in GDP growth since 2004) and the recent discovery of extractable resources will increase Cambodia's revenues by at least one order of magnitude in coming years. Chevron is likely to begin pumping oil and gas in about 2010 or 2011, while foreign mining firms will begin extracting gold and bauxite from the ground in roughly the same time frame. Not only are there other blocks of potential oil and gas in the Gulf of Thailand, there are other mining projects, including coal, iron and gems, that could develop into large-scale enterprises. The challenge will be to find ways to channel the revenues into programs that help the Cambodian people and reduce poverty. A starting point would be Cambodia's signing on to the Extractive Industries Transparency Initiative. Donors are working to reform other areas of government, including financial management, so that the RGC will be better able to handle the new revenue.

The Challenges as We See Them

¶6. (U) Recognizing that eliminating the culture of corruption is a task that will span a generation, we have focused on a limited number of key objectives. Despite occasional pro forma declarations, the RGC has clearly demonstrated that it lacks the political will to attack corruption. Therefore, a key task will be getting the RGC to take ownership of the issue in a serious way. Related to this is obtaining greater transparency in governmental decision-making. The other major focus must be on creating an atmosphere in which systemic corruption is no longer tolerated. This requires increasing public awareness of what constitutes corruption, the cost of corruption, and increased public dialogue on the costs and damage that corruption inflicts on Cambodian society. (A recent poll indicated that 83% of Cambodians believe that they lose less than \$1 a month

to corruption.)

What We Have Been Doing

¶7. (SBU) We have raised our concerns about corruption in general and the "oil curse" in particular at all levels of government, including with the PM, that Cambodia could well become a Nigeria-like country if it does not now begin to implement the needed mechanisms and reforms. The PM has begun to publicly warn against Cambodia becoming "the next Nigeria," but has taken no practical steps to ensure this does not occur.

¶8. (U) In the first phase (2005-2006) of our anti-corruption program, we provided technical assistance to bring the draft anti-corruption law in line with international standards. From a starting point in which virtually no one in civil society dared to publicly address corruption issues, we have helped to create a nationwide coalition of civil society organizations (CSOs) involved in anti-corruption efforts. The Embassy has also worked to build donor consensus on maintaining corruption as a high profile issue that the RGC must address. We launched the "Clean Hand" campaign to raise awareness; 75% of Cambodians now recognize the brand as an anti-corruption symbol. We trained 12 journalists in investigative journalism so that they would be capable of reporting on corruption in an objective manner. They have published 21 exposés of corruption and are mentoring students at the University of Phnom Penh. We encouraged Transparency International to include Cambodia in its rankings; prior to 2005 Cambodia was not listed.

Anti-Corruption Second Phase (2007-2010)

¶9. (U) The second phase will continue multi-pronged tactics to address corruption. A strong focus will remain on getting the RGC to accept responsibility for the issue. Efforts will continue to inform the public about the cost of corruption and to obtain passage of the anti-corruption law. The Mission will seek ways to support policy and regulatory reform to prevent the oil curse. With the end of restrictions on direct assistance to the government, this will include strengthening of ministries, such as Health and Education, that should be recipients of oil revenue so that they will be better prepared to manage the inflow of

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increased revenue. We are launching a strong effort to engage the private sector, local business and multi-national corporations. We will begin working to reduce corruption on a sector-by-sector basis, starting with the easiest sector in order to create a model for other sectors.

Rewards for Good Behavior

¶10. (SBU) One of the key challenges is to convince the Cambodian leadership, which profits most from corruption, that it is in their long-term interest to eliminate graft. The argument can be made that increased foreign investment as a result of a more hospitable environment will create a larger pie that will raise the incomes of all Cambodians and that this would burnish Cambodia's international reputation. It would encourage Cambodians to this way of thinking if they were aware that there could be other rewards for Cambodia if it cleaned house. Specifically, it would be helpful if Cambodian leaders were aware of the Millennium Challenge Corporation's Threshold Program, which Cambodia might qualify for in a few years. We have raised the issue broadly with the Prime Minister, and in greater detail with the Deputy PM, as well as with one of the PM's key economic advisors, but the Cambodian leadership has not followed up. While the Cambodian Embassy in Washington might be utilized to gather

information, the Cambodian Ambassador to the U.S. is not a key political player whose views are accorded great weight. What is needed is a visit by representatives of the Millennium Challenge Corporation to brief senior Cambodian leaders on the Threshold Program. The RGC places great value on Washington visitors and we believe that the reform-minded members of the Prime Minister's economic team would consider an MCC visit a boost to their own efforts in public sector financial reform.

¶11. (U) ACTION REQUEST: Post requests that the Department urge the Millennium Challenge Corporation (MCC) to send representatives of the corporation to Cambodia in order to introduce the Threshold Program to senior Cambodian officials. This visit could be concurrent with a visit to the region by MCC for other purposes. At the same time, we will also encourage senior Ministry of Economics and Finance (MEF) officials to consider a Washington visit that might include meetings with the MCC. From the point of view of RGC optics, however, an MCC visit to Cambodia would carry far greater weight. The stakes for Cambodia and for donor countries are enormous. If Cambodia fails to prepare properly for its oil windfall, the already disturbing chasm between haves and have-nots will profoundly deepen. This in turn will likely lead to greater social and political instability. And we, like other donor states, will continue to expend hundreds of millions of dollars annually to provide basic services to Cambodia's poor, while hundreds of millions of oil revenue dollars are siphoned off by powerful elites.

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